

Message Text

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ORIGIN ARA-20

INFO OCT-01 ISO-00 AID-20 TRSE-00 EB-11 FEA-02 CIEP-02

OMB-01 XMB-07 FRB-02 CEA-02 SS-20 NSC-07 CIAE-00

INR-10 NSAE-00 RSC-01 SP-03 IGA-02 PA-04 PRS-01

USIA-15 /131 R

DRAFTED BY ARA/BC:WLOWENTHAL:BJD

APPROVED BY AA/LA:HKLEINE

ARA/BC:JEKARKASHIAN (DRAFT)

LA/DR:FSCHIECK (DRAFT)

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P 172226Z MAY 74

FM SECSTATE WASHDC

TO AMEMBASSY SANTIAGO PRIORITY

C O N F I D E N T I A L STATE 103921

E.O. 11652: GDS

TAGS:CI, ECON, EFIN

SUBJECT: SAEZ/KLEINE MEETING, MAY 16

1. RESPONDING TO QUERY REGARDING CURRENT SITUATION ABOUT
BALANCE OF PAYMENTS AND INFLATION, SAEZ COMMENTED AS FOLLOWS
REGARDING BALANCE OF PAYMENTS, AN IMF MISSION WAS PRESENTLY
IN CHILE AND WOULD SOON COME UP WITH A NEW ESTIMATE OF THE
GAP. SAEZ SAID THAT THE AVERAGE COPPER PRICE USED FOR
CALCULATING THE GAP WAS 95 CENTS PER POUND. THE AVERAGE FOR
THE LAST MONTH WAS DOL 1.01 AND HIS ESTIMATE FOR THE YEAR IS
DOL 1.06. IF THESE ESTIMATES PROVE OUT, THE BALANCE OF
PAYMENTS PICTURE WOULD BE BETTER THAN CURRENTLY ESTIMATED.
HIS GOVERNMENT'S EARLY ESTIMATES OF COST INCREASES DUE TO
THE ENERGY CRISIS HAVE TURNED OUT TO BE QUITE INADEQUATE.
COST OF FERTILIZERS WITH A PETROLEUM BASE HAS RISEN MUCH
MORE THAN ANTICIPATED. FREIGHT AND OTHER ITEMS DIRECTLY AND
INDIRECTLY DEPENDENT UPON PETROLEUM HAVE INCREASED FAR
BEYOND THE ORIGINAL ESTIMATES. IN ADDITION, THE ABSENCE OF
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CAPITAL INVESTMENT DURING THE ALLENDE PERIOD, PARTICULARLY

IN HYDROELECTRIC EXPANSION, LEAVES NO ALTERNATIVE THAN TO FILL THE GAP WITH THERMAL PLANTS UNTIL HYDROELECTRIC CONSTRUCTION CAN LATER CATCH UP TO THE DEMAND. THIS NEW INVESTMENT IS ESSENTIAL TO AVOID FORESEEN POWER SHORTAGES.

2. MR. KLEINE SAID THAT HEARINGS ON THE AID BILL WERE SOON TO BEGIN AND THAT IN ANTICIPATION OF THE HEARINGS, HE AND OTHERS HAD BEEN MEETING WITH VARIOUS SENATORS AND REPRESENTATIVES TO INFORM THEM OF THE PROGRAM WE HAVE PROPOSED FOR CHILE FOR FY 75 AND ON OUR INTENTIONS REGARDING RECOMMENCING DISBURSEMENTS ON SELECTED OLD LOANS. WHILE THERE WAS LITTLE REACTION TO OUR SPECIFIC PROPOSALS, MUCH INTEREST WAS EXPRESSED IN THE OVERALL POLITICAL PICTURE. MR. SAEZ SAID HE UNDERSTOOD AND HE HOPED THAT THE IMAGE WAS IMPROVING AND THOUGHT IT SHOULD.

3. WITH RESPECT TO INFLATION, MR. SAEZ SAID THAT HIS RECOMMENDATIONS TO THE CONTRARY, THE GOVERNMENT HAS NOT CONSIDERED IT POSSIBLE TO CLAMP DOWN AS HEAVILY ON THE INFLATIONARY FORCES AS ECONOMIC NECESSITY REQUIRED. IN FACT, MR. SAEZ SAID HE KNEW OF NO TRADITIONAL METHODS WHICH WOULD WORK TO SUBDUE HYPERINFLATION AND HE RECOGNIZED THAT HUMAN AND POLITICAL CONSIDERATIONS HAD TO BE INCLUDED IN DETERMINING ANTI-INFLATIONARY MEASURES. NEVERTHELESS, EVEN WITHOUT TAKING EXTREME MEASURES, HE FELT MISTAKES HAD BEEN MADE DUE TO THE LACK OF EXPERIENCE OF GOVERNMENT OFFICIALS, PARTICULARLY IN THE CENTRAL BANK. HE THOUGHT A LOWER SUBSIDY RATE COULD HAVE BEEN WORKED OUT ON PRIMARY FOODSTUFFS AND THAT STRICTER CONTROL SHOULD HAVE BEEN APPLIED TO THE PRINTING OF MONEY. HE ALSO THOUGHT THAT THE POLICY HAD BEEN TOO LIBERAL IN GRANTING REQUESTS FOR LOANS TO DOMESTIC INDUSTRIES, ESPECIALLY THOSE WITH HIGH INVENTORIES. ALL OF THESE CONTROL SLIPPAGES LED TO A MUCH HIGHER ANNUAL RATE OF INFLATION THAN ANTICIPATED AT THE BEGINNING OF THE NEW GOVERNMENT. HE FELT THAT THE ANNUAL RATE WOULD BE BETWEEN 200 AND 250 PCT ALTHOUGH IN PUBLIC HE WOULD HOLD TO HIS EARLIER ESTIMATE OF 150#. HE ADDED THAT HE WAS CONVINCED THAT THE TRUE RATE FOR ALLENDE'S LAST YEAR WAS MUCH HIGHER THAN THE OFFICIAL FIGURE OF 650#. HE THOUGHT IT WAS CLOSER TO 1200

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OR 1300# WHICH MEANS THAT A DECREASE TO 200 OR 250# ATTESTS TO THE GREAT EFFORT OF HIS GOVERNMENT. NONETHELESS, MUCH MUST BE DONE TO REDUCE IT TO A MORE MANAGEABLE RATE. THE IMPACT OF SUBSTANTIALLY HIGHER IMPORT COST OF FUEL, OIL-RELATED PRODUCTS, AND FOOD WAS OF COURSE ANOTHER MAJOR INGREDIENT.

4. MR. KLEINE SAID THAT AID WAS NOW PREPARED TO BEGIN DIS-

CUSSIONS WITH THE APPROPRIATE CHILEAN AUTHORITIES ON THE MATTER OF DISBURSEMENTS ON OLD LOANS AND THAT WE WOULD BE PROVIDING OUR MISSION APPROPRIATE GUIDANCE. WE ENVISAGED THAT THE MISSION WOULD REVIEW THE LOANS ON A CASE-BY-CASE BASIS WITH THE GOC AND MAKE RECOMMENDATIONS TO WASHINGTON WHERE THE FINAL DECISIONS WOULD BE MADE. HE NOTED THAT WE WOULD HAVE TO KEEP IN MIND THE CONGRESSIONAL INTEREST IN AVOIDING A LONG STRETCH-OUT OF LOANS. MR. SAEZ SAID HE WAS PLEASED AT THIS NEWS AND WAS SURE THAT HIS GOVERNMENT WOULD COOPERATE FULLY WITH AID IN THIS UNDERTAKING.

5. MR. KLEINE MENTIONED THAT WE HAD DECIDED TO INCLUDE THE 40-YEAR LOANS IN OUR BILATERAL DEBT RESCHEDULING AS AN ADDED EFFORT TO HELP THE GOVERNMENT'S ECONOMIC STABILIZATION REHABILITATION PROGRAM. MR. SAEZ COMMENTED THAT HE WAS MOST GRATEFUL FOR THIS ADDITIONAL ASSISTANCE WHICH WAS MUCH NEEDED. HE ADDED THAT HE INTENDED TO CONSIDER REOPENING NEGOTIATIONS WITH THE UK TO TRY TO REDUCE THE INTEREST OF 7-1/2# WHICH HE HAD HEARD HAD BEEN ACCEPTED BY CERTAIN OF HIS GOVERNMENT'S AUTHORITIES. HE IMPLIED THAT THIS HAD BEEN DONE WITHOUT HIS KNOWLEDGE AND HE WAS LOOKING INTO THE MATTER FURTHER. HE SAID HE UNDERSTOOD THE PROBLEM THIS CREATED FOR THE U.S. NEGOTIATORS AND HE WOULD DO HIS BEST TO MAKE IT POSSIBLE TO SETTLE, AS ORIGINALLY PLANNED, ON A 6# RATE.

#READ AS PERCENT. RUSH

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